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**BEFORE THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF CALIFORNIA**

Application of California-American Water
Company (U-210W) for Authorization to Modify
Conservation and Rationing Rules, Rate Design,
and Other Related Issues for the Monterey
District

Application No. 15-07-019
(Filed, July 14, 2015)

**CALIFORNIA-AMERICAN WATER COMPANY AND MONTEREY PENINSULA
WATER MANAGEMENT DISTRICT'S REPLY COMMENTS CONCERNING THE
SETTLEMENT ON THE ANNUAL CONSUMPTION TRUE-UP PILOT PROGRAM
AND ON THE MODIFICATION TO MONTEREY DISTRICT RULE 14.1.1 AND
TARIFF SCHEDULE MO-14.1.1**

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Dated: July 13, 2016

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I. INTRODUCTION

Pursuant to Rule 12.2 of the California Public Utilities Commission ("Commission") Rules of Practice and Procedure, California-American Water Company ("California American Water") and the Monterey Peninsula Water Management District ("MPWMD") (collectively "the Parties")¹ files these Reply Comments to the Comments of the Office of Ratepayer Advocates ("ORA") and Public Trust Alliance ("PTA")² on the *Settlement Agreement between California-American Water Company and the Monterey Peninsula Water Management District on the Annual Consumption True-Up Pilot Program and on the Modification to Monterey District Rule 14.1.1 and Tariff Schedule MO-14.1.1*.

The Settlement Agreement between California American Water and MPWMD proposes (1) the adoption of California American Water's modified water shortage contingency plan, Rule and Schedule 14.1.1 for the Monterey District, and (2) the approval of the Monterey pilot

¹ California American Water files these Reply Comments on behalf of MPWMD and provides electronic signatures in accordance with Rule 1.8 of the Commission's Rules of Practice and Procedure.

² ORA, Public Water Now ("PWN") and Regulatory Liaisons ("RL") also filed Oppositions to the Motion to approve the settlement agreement. All of ORA's arguments in its Opposition are also included in its Comments. California American Water, therefore, will not seek leave to file a reply to ORA's Opposition. California American Water will also note where PWN/RL's arguments are relevant to this Reply.

program to true-up the consumption level for customers on an annual basis (referred to as the “CAM”). The proposed Rule and Schedule 14.1.1 will demonstrate to the State Water Resources Control Board that California American Water will be able to comply with existing and future reductions from the Carmel River. The proposed CAM is a component of California American Water’s attempt to address large under-collected WRAM balances that need to be addressed to ensure revenue stability and avoid harmful impacts on customers.

On the proposed Rule and Schedule 14.1.1, all the commenting parties stated that there should be a Tier 2 Advice Letter when moving from Level 1 to Level 2 Conservation Rates in Stage 3, and that customers should receive notice of the increase. California American Water agrees. California American Water and MPWMD agree the proposed Rule and Schedule 14.1.1 should be amended to reflect those changes.

On the proposed CAM, ORA suggests that the WRAM is functioning properly, any problem was caused by California American Water’s rate design, California American Water has provided conflicting consumption data, and action on the CAM should be delayed because ORA’s proposed rate design somehow will solve the undercollection problem or the Commission will address it in another Rulemaking. ORA’s arguments ignore the importance and urgency of the situation for the Monterey District and the need to adjust rates more frequently to prevent further under-collected balances. The water supply solution must be addressed now, and, as District General Manager David Stoldt and others in this proceeding have argued, the rate design must be fixed and a mechanism put in place to adjust the underlying demand numbers to recover not only the WRAM but other surcharges, including those tied to the Monterey Peninsula Water Supply Project (“MPWSP”). The CAM is a simple and straightforward program that would provide meaningful benefits with a minimum of effort.

With the limited revisions to the proposed Rule and Schedule 14.1.1, California American Water and MPWMD request the Commission adopt the Settlement Agreement in its entirety.

II. DISCUSSION

A. Standard of Review for Adoption of a Settlement Agreement

In light of ORA's and PWN/RL opposition and commentary on the Settlement Agreement, a brief comment on the standard of review of a Settlement Agreement appears necessary. The Commission has a strong policy in favor of settling contested issues. In reviewing proposed settlements, the Commission has consistently reiterated for nearly twenty years that there is a strong public policy favoring settlement of disputes if they are fair and reasonable in light of the whole record. The fact the Settlement Agreement is contested does not alter the ultimate standard of review. "The appropriate standard of review is whether the contested settlement generally *balances the various interests at stake*, not whether it reflects a reasonable accommodation of the *litigation positions of all parties*."³ Notwithstanding the objections by ORA, PWN and RL, and as set forth in the Motion and below, the Settlement Agreement meets the Commission's standard for adoption of a settlement agreement.

B. The Parties to the Settlement Represent a Reasonable Range of Interests

ORA argues that California American Water and MPWMD "do not represent ratepayer interest in this proceeding" and that the proposed settlement is not "fairly representative of affected interests."⁴ California American Water and MPWMD object to ORA's assertion that the Settlement Agreement does not represent ratepayer interests. The Settlement Agreement provides two critical pieces to California American Water's overall plan to address the pending "physical-cliff" of the State Water Resources Control Board's 2009 Cease and Desist Order⁵, ensure revenue stability, and avoid harmful impacts on customers. The proposed Rule and Schedule 14.1.1 will assist California American Water in complying with the CDO by providing a clear and defined path for sending conservation signals to customers and implementing rationing, if necessary. Customers would benefit from the CAM in particular by reduction in surcharges, more consistent and timely price signals, and lowered rates due to shorter periods for WRAM balances to accrue interest.⁶ The CAM will also provide more revenue stability, which

³ D.07-11-018, 2007 Cal. PUC LEXIS 27 at *13 (emphasis added).

⁴ ORA Comments, p. 3.

⁵ SWRCB Order WR 2009-0060, October 20, 2009.

⁶ Exh. 9, Linam Direct, p. 25.

is crucial to achieve low cost financing for the MPWSP⁷, another benefit to ratepayers. Even if ratepayer interests were not represented in the Settlement Agreement, which they are, the Commission has previously adopted settlement agreements that did not include the sponsorship of ORA or any other ratepayer interest group.⁸ Here, the Settlement Agreement is supported by the utility and local government body, whose mission “is to promote or provide for a long-term sustainable water supply, and to manage and protect water resources for the benefit of the community and the environment.”⁹ The Settlement Agreement, therefore, represents a reasonable range of interests. The fact that the Settlement Agreement did not have the sign off of ORA, PWN/RL, or PTA is not grounds for the Commission to reject it.

C. Settlement on Rule and Schedule 14.1.1

California American Water inadvertently omitted from the proposed Rule 14.1.1 a requirement to file a Tier 2 Advice Letter when moving from Level 1 to Level 2 Conservation Rates in Stage 3. California American Water agrees that it should file a Tier 2 Advice Letter when moving from Level 1 to Level 2 Conservation Rates in Stage 3, and that customers should receive notice of the increase. Attached as Exhibit A is a copy of Rule and Schedule 14.1.1 which reflects the changes California American Water believes are being proposed by the commenting parties. California American Water and MPWMD agree the proposed Rule and Schedule 14.1.1 should be amended to reflect those changes.¹⁰

PWN/RL asserts the Settlement, which incorporates the MPWMD rationing program, provides too much water to small households with 1 or 2 persons and too little water to households with 4 or more people. Contrary to PWN/RL’s opinion, MPWMD engaged in a

⁷ Exh. 204, Stoldt Direct, pp. 10-11.

⁸ D.10-12-016, *Decision Approving Regional Project, Adopting Settlement Agreement and Issuing Certificate of Public Convenience and Necessity for California-American Water Facilities*, pp. 56-57; D.06-02-033, *Application of PacificCorp (u-901-E) and MidAmerican Energy Holdings Company for Exemption Under Section 853(b) from the Approval Requirements of Section 854(a) of Public Utilities Code with Respect to the Acquisition of PacificCorp by MidAmerican*, 2006 Cal. PUC LEXIS 49, *66.

⁹ <http://www.mpwmd.net/who-we-are/mission-vision-goals/mission-statement/>

¹⁰ PWN/RL also argues that the Settlement Agreement should be denied for the additional reason that the proposed Rule and Schedule 14.1.1 deliver “no Conservation Signal to Non-Residential Customers.” (PWN/RL Opposition, p. 3.) PWN/RL is incorrect. The Rule and Schedule applies to all Customers and there is Non-Residential water rationing in Stage 4.

public process that included at least two public hearings as well as multiple workshops, some with California American Water, seeking public input prior to adopting Ordinance No. 169.

Furthermore, MPWMD has had an established minimum ration of 35 gallons per person per day (gpppd) since late 2008.¹¹ This was based on the 2008 Drought Urban Guidebook published by the State of California, Department of Water Resources, Office of Water Use Efficiency and Transfers which applies to interior residential use. With regard to larger average households, it was assumed that certain efficiencies occur with food preparation, dishwashing and laundry that would not require a full ration for each additional person. All of these numbers and how they were derived were vetted through a public process.

D. Settlement on Annual Consumption True-Up Pilot Program

1. The CAM is Necessary and ORA's Proposed Rate Design Will Not Fix The Problem.

Contrary to the Comments filed by ORA and PWN/RL, the CAM is necessary to fix the very real problem of ballooning WRAM balances. Indeed, the CAM is the linchpin of the plan to stabilize revenues, avoid future large undercollected WRAM balances, and maintain the ability to finance the MPWSP on terms most beneficial to customers. Without the CAM, California American Water and its customers will likely find themselves again facing substantial undercollections of authorized revenues tracked in the WRAM.¹²

ORA states that that the “high WRAM balance resulted from Cal Am’s allotment rate design and lack of management oversight of the allotment system. These flaws have been addressed in ORA’s rate design proposal in this proceeding.”¹³ ORA does not – because it cannot – provide any explanation of how its own deeply flawed rate design actually fixes the ballooning WRAM balance in a timely manner. Moreover, ORA’s proposed consumption-based allocation is unprecedented and untested; ORA admitted under cross-examination that it was unaware of any Commission-regulated utilities employing a rate design that bases allocation of

¹¹ See MPWMD Ordinance No. 137 effective December 31, 2008. Given the improvements in water fixture technology currently available, a reduction to 30 gpppd is not unreasonable.

¹² Exh. 11, Linam Rebuttal, pp. 17-20.

¹³ ORA Comments, p. 3.

recovery of revenues solely on consumption as ORA recommends.¹⁴ ORA's proposal is also inherently illogical, as it apportions fixed costs to each class based on the proportion of total consumption despite the fact that fixed costs, by their very nature, are incurred independent of consumption.¹⁵ ORA's proposed allocation also appears to result in non-residential customers subsidizing residential customers, contradicting one of the most basic principles of rate design.¹⁶ ORA's rate design will not solve the challenges facing the Monterey District.

ORA also argues that "Cal Am's mismanagement of its allotment rate has prevented the timely recovery of the revenue requirement and contributed to the WRAM balance, but has not demonstrated that the WRAM itself hinders timely adjustment of rates nor hinders the collection of Cal Am's authorized revenue requirement."¹⁷ First, California American Water and MPWMD are not saying that "the WRAM itself hinders timely adjustment of rates nor hinders the collection of Cal Am's authorized revenue requirement." The problem is that the complex and highly volatile rate design in the Monterey District has made it impossible to recover authorized revenues in a timely manner, leading to large (\$50,626,735 through December 31, 2015)¹⁸ undercollected WRAM balances. Furthermore, Tier 1 usage (which represents nearly 60% of residential usage) is currently excluded from amortization of the WRAM balance for residential customers in Monterey, which has led to a situation where the WRAM cannot be fully recovered and continues to grow. While adopting California American Water's rate design will help, without the CAM, the Company and its customers will likely be facing ballooning WRAM balances again in short order.

Second, ORA's claim that California American Water mismanaged "its allotment rate" is not only an extraordinarily vague statement, it is also unsupported and demonstrably false. ORA has repeatedly supported the allotment based rate design, even when California American Water, with the support of MPWMD, sought to modify it so that the residential allotments played a

¹⁴ ORA admitted that it was unaware of any Commission-regulated utilities making such an allocation. See Exh. 14, Response to CAW-ORA-002-Q001; RT 935: 22-27 (Odell/ORA). In its research, California American Water was unable to find any examples of such a practice.

¹⁵ Exh. 7, Chew Further Rebuttal, p. 9.

¹⁶ Exh. 7, Chew Further Rebuttal, p. 9.

¹⁷ ORA Comments, p. 4.

¹⁸ See California American Water Advice Letter No. 1211.

lesser role.¹⁹ Throughout the last decade and a half of ORA support, the per capita rate design and residential household allotment process have had the same defining features: (1) reliance on self-reported information (which will always have a certain degree of inaccuracy), (2) no independent verification by California American Water, (3) no authority for California American Water to compel information from its customers,²⁰ and (4) the power to impose penalties for misreporting lies solely with MPWMD.²¹ As Ann Bui, Black & Veatch Managing Director and water industry expert, concluded, “[b]ased on our review of the Company’s policies, procedures and provided billing data as well as interviews with more than a dozen Company employees, in my opinion the Company has not mismanaged the allotment system.”²²

More importantly, it is unclear why ORA believes that residential allotment inaccuracies (real or imagined) could lead to a multimillion dollar WRAM undercollection. The only way that inaccurate residential household allotments could possibly materially affect the WRAM is if the allotments used for billing were significantly different from the allotments used to develop the authorized revenue requirement, thus preventing recovery of the authorized fixed costs. The same residential household allotments were used, however, to develop the rates, rate design, and authorized revenue requirement, and they have not substantially changed over time.²³

ORA’s argument that California American Water mismanaged its allotment based rate design and that ORA’s rate design will fix the problem has no merit. ORA’s argument should be rejected and the Settlement Agreement adopted.

2. The CAM Does Not Result in Single-Issue Ratemaking or Create Inequitable Treatment Across Customer Classes.

ORA also argues the CAM should not be adopted because it adjusts rates without taking into consideration all of the factors identified in Public Utilities Code section 727.5(a)²⁴, and

¹⁹ Exh. 13, Stephenson Rebuttal, p. 8.

²⁰ RT 855:2-28 (Stephenson/CAW); Exh. 13, Stephenson Rebuttal, Attachment 3.

²¹ RT 566:24-26 (Stoldt/MPWMD).

²² Exh. 6, Bui Rebuttal, p. 17.

²³ Exh. 7, Chew Further Rebuttal, Attachment 2.

²⁴ Section 727.5(a) provides: “In establishing rates for water service, the commission shall consider, and may establish, separate charges for costs associated with customer service, facilities, variable operating

results in single-issue ratemaking and treats different classes of customers inequitably.²⁵ This argument is based on a fundamental misunderstanding of the CAM. As California American Water has explained, it is not proposing to engage in rate design through the CAM or develop a new consumption forecast through the CAM's proposed advice letter process; there is no need to review fixed and variable costs, or other factors identified in Public Utilities Code section 727.5(a). Under the proposed CAM, actual recorded consumption would simply replace the adopted quantities and be used for rate adjustments for the one-year period until new recorded consumption data is available. ORA provides no explanation for why it would be necessary to consider all the factors in Section 727.5(a) before adjusting the rates based on actual recorded consumption data.

ORA's and PWN/RL's argument that the CAM cannot be adopted because it creates disparate impacts is flawed. There is nothing that precludes California American Water from charging different classes of customers different amounts based on cost of service. ORA's argument would only make sense if the Commission were to accept the underlying premise in ORA's unprecedented consumption-based allocation, which demands that every customer pay the exact same cost for every unit of water. As stated above, ORA's argument and rate design fails to take into account the realities of water service. For example, every customer receives a bill. The cost to read the meter and print and mail the bill is the likely the same, regardless of how much water they consume. Since residential customers comprise 86% of the Monterey main system customer base, 86% of the billing costs are driven by these customers, regardless of how much water they consume.²⁶ It would simply not be equitable to allocate this fixed cost based on consumption, as ORA proposes. As stated above, ORA's proposed allocation results in non-residential customers subsidizing residential customers, contradicting one of the most basic principles of rate design. It is ORA's rate design that would create inequities, not the proposed CAM.

costs, including fixed and variable costs associated with supplying the water, or other components of the water service provided to water users.”

²⁵ ORA Comments, pp. 5-6.

²⁶ Exh. 7, Chew Further Rebuttal, p. 9.

Again, ORA's proposed rate design will not fix the urgent problem the CAM is designed to fix. There is nothing in Section 727.5, or any other authority cited by ORA that precludes adoption of the proposed CAM.²⁷

3. The CAM Will Not Encourage Customer Consumption

ORA argues that the CAM could encourage customers to "increase consumption at times when the Monterey District is in need of increased conservation from its residents."²⁸ ORA's concerns are unfounded because the Monterey District tiered rate design would continue to send a strong conservation signal. Moreover, there are use restrictions that would be activated under Rule and Schedule 14.1.1, including the imposition of penalty rates, if customers chose to stop conserving.²⁹ Given the water supply constraints in the Monterey District, including the need to comply with the SWRCB's strict demand limits now and in the future, an increase in demand from customers as a result of the CAM is highly unlikely.³⁰

4. Commission Review of California Water Service's Sales Recognition Mechanism is not Required to Approve the CAM

ORA argues the CAM cannot be adopted because D.15-04-007 "states that the Commission would not authorize any further pilot programs until it has reviewed [California Water Service's ('CWS') Sales Recognition Mechanism ('SRM')] pilot program."³¹ In D.15-04-007, the Commission specifically allows California American Water to seek authorization for a

²⁷ In its Opposition PWN/RL states the use of a heretofore unheard of "Mixed Use" customer class is reason to reject the CAM. "Mixed Use" as a customer class has been around for a long time, and applies to customers who have both residential and nonresidential use through a common meter. Furthermore, because California American is requesting to eliminate the individual allotment based rate design, there was a need to change the billing category in which the "Multi Residential" Customer category is billed. PWN/RL further argues that the Settlement Agreement should be rejected because Resale and Construction customers are excluded from the CAM. Resale and Construction customers are not only a very small customer category with very limited consumption, but they are also billed on standard rates and do not qualify for a WRAM. With no WRAM undercollection attributable to them, there is no basis to include them in the CAM. PWN/RL also argues that the exclusion of "Variable Expenses" from the CAM is grounds to deny the Settlement Agreement, but those expenses are very small and can easily continue to be tracked in the MCBA without creating any significant difference in the account balance.

²⁸ ORA Comments, p. 6.

²⁹ Exh. 11, Linam Rebuttal, p. 17.

³⁰ *Id.*

³¹ ORA Comments, p. 7.

consumption adjustment mechanism in an application (such as this one) filed prior to the next general rate case.³² ORA also argues that because it found fault with CWS's SRM, the CAM should not be authorized.³³ The CAM that California American Water and MPWMD are proposing is, however, significantly less complex than CWS's SRM or the ORA/California American Water SRM from the last general rate case.³⁴ There is nothing in D.15-04-007 or ORA's extra-record evidence regarding its review of the CWS's SRM that suggests the CAM is not necessary and appropriate.³⁵

5. The Proposed CAM is Urgently Needed Now and Narrowly Tailored to Monterey

ORA also argues that the Commission should not approve the CAM because the Commission is considering true-up mechanisms more broadly as part of another proceeding (R.11-11-008).³⁶ The CAM is simple, narrowly crafted, and applicable only the Monterey District. Thus, there is little risk that "potential conflicts" by adopting the proposed CAM prior to any decision in R.11-11-008. Indeed, during the workshops in R.11-11-008, both California American Water and MPWMD emphasized that while it may be appropriate to consider the need for consumption true-up mechanisms generally in that rulemaking, the issues in Monterey are unique and need to be addressed in this proceeding.³⁷ Moreover, although the R.11-11-008 schedule originally provided for a decision no later than October 2016,³⁸ the dates for serving testimony were deferred and the evidentiary hearings were taken off calendar.³⁹ California American Water reached the settlement with MPWMD because of the urgent need to address its rate design and WRAM balances in the Monterey District. Given the limited applicability of the

³² *Ibid.*

³³ ORA Comments, p. 8.

³⁴ RT 456:4-5 (Linam/CAW).

³⁵ PTA suggests the Commission "consider whether it is appropriate to make use" of CWS's SRM. California American Water believes the CAM is a much simpler, less complicated version of the SRM and does not believe it would be appropriate to apply the CWS SRM to the Monterey District at this time.

³⁶ ORA Comments, p. 8.

³⁷ Exh. 11, Linam Rebuttal, p. 12.

³⁸ R.11-11-008, Administrative Law Judges' Ruling Setting Workshop and Further Schedule in R.11-11-008, September 14, 2015, Attachment D.

³⁹ R.11-11-008, Assigned Commissioner's Ruling Regarding Comments and Reply Comments on the October 2015 Workshop Report, November 6, 2016, p. 3.

proposed CAM, there is no need to reject the settlement to wait for the results of a rulemaking, which is currently dormant.

6. There is No Record of Conflicting Consumption Data

ORA argues that “the Commission cannot allow Cal Am to adjust rates using the CAM based on the prior year’s consumption data” because “[t]he record in this proceeding demonstrates that Cal Am has provided inconsistent consumption data on numerous occasions” and “demonstrated it has a practice of delaying the recording of consumption data and then utilizing that data to its benefit.”⁴⁰ PWN/RL and, to a lesser extent, PTA join in this argument.⁴¹ ORA’s argument is, however, unfounded. The alleged inconsistencies are created by ORA itself. As California American Water demonstrated, “ORA pulls numbers from several reports that are used for different purposes or present consumption for different classes to try to show conflicts.”⁴² In its attempt to show conflicts, ORA has included settlement data based on a four-year historical average, has attempted to compare consumption for the Monterey Main system with consumption that also includes the Bishop, Hidden Hills, and Ryan Ranch systems, and misrepresented information provided by California American Water in response to a data request.⁴³ Additionally, the Rebuttal Testimony of Sherrene Chew in no way supports a claim that California American Water has a practice of delaying consumption data and utilizing it to its benefit. ORA cites to page 14 of Ms. Chew’s testimony as evidence of California American Water’s intentional delay in recording consumption data for its benefit, but there is nothing on page 14 that supports ORA’s statement.⁴⁴ The issues that ORA raises do not justify rejecting the

⁴⁰ ORA Comments, p. 9.

⁴¹ PTA “supports a methodology that allows Cal-Am to utilize the most current consumption data to estimate future demand and to set rates,” but based on ORA’s arguments on “inconsistent consumption data,” believes “ample time to scrutinize the data for accuracy” should be incorporated in to the CAM.

⁴² Exh. 11, Linam Rebuttal, p. 22.

⁴³ *Id.*, pp. 22-23, referring to Exh. 104, ORA Report, Table 3-A.

⁴⁴ In its Opposition, PWN/RL also accuses California American Water Company of providing conflicting data and intentionally filing its 2015 Annual Report in order to “deny knowledge of the decrease [in production] to PWN and RL for this submission.” On the issues of conflicting data, PWN/RL points to no specific example of California American Water providing conflicting data. There is no evidence of any conflict. As to the filing of the 2015 Annual Report, on February 11, 2016, California American requested from the Commission, and subsequently received from the Commission, an extension of time to file its annual report. As a subsidiary of the American Water Works Company, California American Water’s audited financial statements follow the audited financial statements of its parent company and

CAM, and do not justify requiring California American Water to “make all requests for rate adjustments via formal application or general rate case proceeding.”⁴⁵

III. CONCLUSION

For the reasons set forth in detail above, California American Water and MPWMD respectfully request the Commission disregard the Comments supplied by ORA, PWN/RL and PTA and instead adopt the Settlement Agreement, as revised, in its entirety.

Respectfully submitted,

Dated: July 13, 2016

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California American Water would not have had time from the date the subsidiary financial statements are available to prepare the report.

⁴⁵ ORA Comments, p. 9.